A Review of the Texas Economy from the Office of **Susan Combs, Texas Comptroller of Public Accounts** • May 2011

# FISCAL NOTES

MARCH REVENUE (IN MILLIONS): SALES TAX: $1,616.3 OIL PRODUCTION: $96.2 NATURAL GAS: $112.6 MOTOR FUELS: $229.3 MOTOR VEHICLE SALES: $285.8 TOBACCO: $137.8

INSIDE STORIES



## The Oil Beneath the Oil

*Texas University Seeks to Revive Oilfields* **SEE PAGE 8**

## LETTER FROM THE COMPTROLLER

AS COMPTROLLER, I've had the opportunity to travel to cities, suburbs, small towns and farming communities in every corner of our state. Whether I'm in the Panhandle, down in the Valley or any place from El Paso to Texarkana, it's always clear that Texans have an intense pride in our great state and their unique place in it.

And every community, no matter how big or small, is centered on local businesses, and the men and women whose investments and sweat equity have made them respected institutions on Main Streets all over Texas.

They're the moms and pops whose stores have weathered the economic challenges of the recent recession. They're the barbers, bankers and bakers who sponsor Little League teams and proudly put their names on those Fourth of July floats. They're the stores staffed by stock boys or checkout girls who may someday become tomorrow's CEOs. And the local sales taxes they collect are returned to their communities to finance public safety and other vital services.

In this issue of *Fiscal Notes,* we take a look at our recent FAST report, which scores how local school districts use their financial resources to educate our kids. As government budgets at all levels continue to tighten, we need the same discipline, insistence on efficiency and attention to the bottom line found in our small businesses.

In addition, we look at how corporations have adapted to the Sarbanes-Oxley financial reporting requirements. Transparency — in this case, ensuring accountibility to stockholders — is always a good thing in my book, although the legislation has added some costs to business.

All businesses, whether they employ five or 5,000, want fairness and some measure of certainty. Providing that is one measure of the pro-business environment Texas strives to offer to those who create our jobs — and make the free market work for all of us.

Susan Combs



## ACROSS TEXAS

› **Scott & White Healthcare** has begun building a 320,000-square-foot hospital facility in College Station. When it opens in 2013, the $165 million, 143-bed facility will offer an emergency room, operating rooms, an imaging center, cancer services and interoperative robotics. The project will bring about 600 jobs to the area.

› Medical device maker **Kinetic Concepts Inc.** has announced plans to build a three-story, 100,000-square foot corporate headquarters in northwest San Antonio. The new HQ will open in summer 2012.

› **Disney Cruise Line** will begin offering cruises from Galveston in September 2012. The seven-night cruises will visit ports including Cozumel and Grand Cayman Island and Cozumel.

› **Dish Network** purchased Dallas-based **Blockbuster Inc.** for $320 million in an April bankruptcy auction.

**Visit *FiscalNotes.com* to get e-mail alerts on our publications and up-to-the-minute news on the Texas economy.**




# Texas Entrepreneur Acts Naturally

BY DAVID BLOOM

*Green Exports Keep Company in the Black*

Naturally, every successful entrepreneur needs a good idea. For Lafe Larson, it was only natural for him to go natural — and organic.

Since 1997, when Larson started Lafe's Natural Body Care by selling mineral-salt "deodorant stones" out of a spare bedroom, natural and organic products have grown in popularity, both in the U.S. and around the world.

Today, natural body care is a vibrant $785 million industry growing at a 15 percent clip annually. The products have spread from new-agey health stores to the aisles of your neighborhood grocery stores and pharmacies. That's because today's consumers are increasingly aware of potential health risks from the chemicals commonly found in personal care products. The growing popularity of all-natural body care products is an outgrowth of the overall health and wellness movement as well as growing concerns about the impact of chemicals on the environment.

Larson's popular line of baby products has earned the U.S. Department of Agriculture's (USDA's) National Organic Program (NOP) green seal, because 95 percent or more of their ingredients are organic. In addition, the packaging uses "baby-safe plastic" and is free of potentially harmful chemicals. Products with the NOP designation must be manufactured in a facility that adheres to USDA rules dictating how materials are received, warehoused, mixed and sanitized. All of Larson's products are produced in facilities in McAllen and Dallas that meet these exacting standards.

U.S.-made organic personal care products are particularly desirable in global markets. "They're viewed as being of premium quality," says Larson, who has seen his company's export sales rise 25 to 30 percent annually for the past three years.

Canada remains his largest international customer, but today Larson sells his products to more than 30 countries. In 2010, he completed a deal with a Chinese distributor to provide an organic bug spray, and the distributor has applied for the government import licenses needed to bring 12 other Lafe's products to China in the coming months. The company also recently shipped its first order to a new account in Slovenia in 2010.

Larson, who uses the U.S. Department of Commerce's International Buyer Program to establish relationships with global distributors, says that Lafe's Natural Body Care revenues from exports topped $300,000 in 2010. **FN**

For more information on Lafe's Natural Body Care, visit *www.Lafes.com*.

### THE NATURAL PERSONAL CARE INDUSTRY — QUICK FACTS

U.S. SALES OF NON-FOOD NATURAL PRODUCTS TOPPED

**$56.7 BILLION**

IN 2009, REGISTERING

**9.7% GROWTH**

FOR THEYEAR.

TOTAL GROWTH IN THE NON-FOOD NATURAL PRODUCTS INDUSTRY IS EXPECTED TO AVERAGE ABOUT

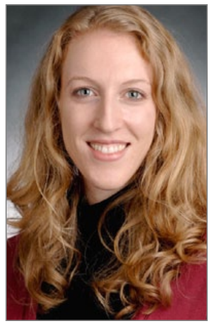
**12% ANNUALLY**


Do you know of a smaller Texas company that is making strides in cultivating international sales? Let us know at *fiscal.notes@cpa.state.tx.us* — we might profile it in an upcoming issue.

BY MICHAEL CASTELLON

# Sarbanes-Oxley, Eight Years On

## *How a Major Reform of Corporate and Finance Law Affected Business*



Genevieve Beyea
Assistant Professor
Texas Tech University
School of Law

The booming economy of the 1990s ended abruptly with the arrival of the new millennium — and the revelation that a number of large, publicly held U.S. companies had fraudulently misrepresented their earnings and financial statements. Investors panicked as the breadth and scale of this fraud became clear, with crippling effects on the U.S. economy.

Congress approved the Sarbanes-Oxley Act of 2002 in the wake of these high-profile accounting scandals. Since then, the law has played a significant role in enhancing corporate and financial accountability and federal oversight.

In this issue of *Fiscal Notes,* we speak with Genevieve Beyea, an assistant professor at the Texas Tech University School of Law, on how Sarbanes-Oxley has affected businesses throughout the U.S.

Beyea, a New York University School of Law graduate who teaches securities regulation and mergers at Texas Tech University, has written extensively on corporate law and acquisitions.

**FN: For the uninitiated, what is the Sarbanes-Oxley Act of 2002?**

**Genevieve Beyea:** Sarbanes-Oxley does a number of things aimed at improving corporate accountability and public company accounting practices. Among the most important of its provisions is the establishment of an oversight board for accounting firms. Another is the "whistleblower" provision, which protects employees who report accounting or audit problems to audit committees or the Securities and Exchange Commission (SEC).

> "The rest of the world is looking to the U.S. because we have such a thorough set of financial regulations."
>
> — Genevieve Beyea
> Assistant Professor , Texas Tech University School of Law

When the dot-com bubble burst, at about the time of the Enron and WorldCom scandals, there was a backlash against fraud and some of the really bad ways in which some of the markets were working. A number of very big companies went under. Enron, in 1999, was the seventh-largest corporation in the U.S. by market capitalization, so when it went under there was a *huge* shock to the system, in the sense that no one saw this coming until it was too late.

It turned out that a lot of [Enron's] assumptions about its future profitability were essentially made up. Investors became fearful of the market and the public became very angry. When that happens, there's often public pressure to do something, and Sarbanes-Oxley was Congress' response.

**FN: And what does the law do?**

**GB:** A number of things. For one, it created an oversight board for accounting firms. And all public companies were required to establish *independent* audit committees. For some companies, this meant hiring new directors. Audit committees can't be made up of directors who are also officers or other employees of the company. So director independence became a big focus.

In addition to that, Sarbanes-Oxley puts increased responsibility on chief financial officers and chief executive officers in terms of financial accountability. It puts more pressure on the CEO to better understand the finances of his or her company.

**FN: What were some of the criticisms of this?**

**GB:** One of the big criticisms was that it pulls the CEO away from the strategic vision and management of the company, and more toward ownership and oversight of finances. CEOs are now deeper in the nitty-gritty of financial reporting.

**FN: How has Sarbanes-Oxley affected the business climate?**

**GB:** The initial cost — the initial investment needed to put systems in compliance — is often very large. But once that's done, the annual ongoing costs aren't so bad, except for the increased costs associated with auditing.

Now that most companies have put themselves in compliance, some of that criticism has gone away. Though there's still this liability factor that hangs over the heads of CEOs and CFOs like a big stick.

One additional criticism is that Sarbanes-Oxley disproportionately affects smaller companies, who are less able to bear the increased costs of auditing than larger firms.

Accounting firms have been frustrated with Sarbanes-Oxley because they see it as [making] them responsible for things they normally wouldn't be accountable for. Previously, the same accountants from an auditing firm might work for the company for 20 years. This resulted in deep personal connections, which might result in a biased auditor.

Now, every five years the lead and reviewing partner from the auditing firm must be rotated off the audit, which is intended to eliminate a lot of the conflicts of interest that existed before. This increases the costs of auditing, however, because the new auditing firm employees assigned to the company must essentially relearn information that those being rotated off had already learned.

The portion of the act calling for independent auditors has really caught on as a desirable thing. There's a debate on whether it's working or not, but overall it has caught on with little conflict.

**FN: It seems like a lot of positive things have come from the legislation.**

**GB:** In general, the rest of the world is looking to the U.S. because we have such a thorough set of financial regulations. This is a natural place for countries like China to look when developing their own provisions against corporate fraud.

**FN: Do any corporations stand out as noteworthy examples of compliance with Sarbanes-Oxley?**

**GB:** Most of the big public companies did a good job of getting this done. This is anecdotal, but in one of my courses I use Hewlett-Packard as an example of a company that has done a good job of implementing an independent audit committee and internal control requirements. As a class, we look at HP's annual reports versus those of WorldCom just before its fall.

> "Sarbanes-Oxley… puts more pressure on the CEO to better understand the finances of his or her company."
>
> — Genevieve Beyea

But most public companies complied to the extent they were able, mainly due to penalties for not complying by a certain date. For the most part, companies were ready to comply when the time came.

**FN: The Dodd-Frank Act, passed in 2010, has a lot in common with Sarbanes-Oxley in that it provides sweeping regulatory reform. Can you talk a little about that?**

**GB:** It's a big piece of legislation similar to Sarbanes in that it's a reaction to the recent financial crisis. The Dodd-Frank Act affects every area of financial regulation, including banks, consumer regulations and rules for the governance of public companies. It's very broad, but not being felt yet because most provisions haven't been implemented. Many will be by this spring, though. The effects are going to develop over the next few years.

Hopefully some good things come out of it, but inevitably there will be things that need further work. Many problems in the housing market, for instance, are too complicated to just legislate away.

Some of it comes down to behavior. How do you legislate in a way so people will be risk-adverse and less interested in short-term results? If you want a stock market with long-term, healthy gains, how do you create that? How do you manage that? For example, some people who held stock through the crisis, as long as it wasn't in companies that actually went under, came out better than those who panicked and sold. That's a broad generalization, but it is something people have noticed. **FN**

Professor Beyea's professional profile can be viewed at *www.law.ttu.edu/faculty/bios/beyea*.

BY BRUCE WRIGHT

# Assessing Your Schools, FAST


**P**ublic education is one of Texas state government's largest single expenditures, and perhaps the most important factor in ensuring our continuing economic prosperity. A new report from the Comptroller's office can help Texans learn just what results they're getting for their education dollars.

The 2009 Texas Legislature charged the Comptroller with identifying school districts that combine high academic achievement with cost-effective operations — in effect, to determine which districts are providing a good return on Texans' investment. In response, the Comptroller's office created the Financial Allocation Study for Texas (FAST), an unprecedented look at the link between school funding and academic results.

The Legislature charged the Comptroller with identifying school districts that combine academic achievement with cost-effective operations.

## VITAL SERVICE, BIG COST

In Texas' 2010-2011 budget period, public K-12 schools received about 43.7 percent of the state's general revenue. Our schools also account for a large portion of local government spending, as homeowners recognize whenever they pay their property taxes.

These costs have risen rapidly over the last decade. According to the Texas Education Agency, annual school district spending (including local, state and federal funds) rose by 95 percent between the 1998-99 and 2008-09 school years.

And surprisingly little of this increase was attributable to the state's rapid population growth, as public school enrollment rose by just 19.7 percent over this period. Texas school district spending per student rose by 63 percent between 1998-99 and 2008-09, to $11,567.

In a time of extraordinarily tight budgets, spiraling cost figures such as these make it imperative that our schools spend their tax dollars as efficiently and effectively as possible — hence the FAST study.

## LEVELING THE PLAYING FIELD

Factors other than funding can affect academic performance, of course, and many of these may be beyond school district control.

The Comptroller's FAST team worked with researchers at the state's top universities as well as school district superintendents and trustees to ensure the fairness of its assessments. The methods used allow for numerous factors to ensure *fair and accurate* appraisals of relative school district success.

Academic progress measures used in FAST employ 32 variables, including factors such as student demographics, economic disadvantage and limited English proficiency. The spending assessments, in turn, control for eight variables, including total enrollment,


area labor costs and each district's geographic size.

Based on these measures, school districts throughout the state were assigned a FAST rating ranging from one to five stars. "We found that 43 Texas school districts met the criteria for the five-star rating, producing consistently strong and cost-effective academic growth," says Tom Currah, lead researcher on the FAST project.

School districts throughout the state were assigned a FAST rating ranging from one to five stars.

The FAST report provides an array of best practices from the most efficient and effective school districts that can be used by other districts wishing to improve their operations. It also offers a series of Comptroller recommendations that could save state and local governments millions of dollars while maintaining or improving their academic results.

An accompanying Web-based tool allows users to run custom reports to compare school districts on measures of spending and academic success.

"The Web tool lets you review Texas Education Agency ratings and statistics as well as the new FAST indicators, for any district you choose," says Beth Hallmark, who oversees the Comptroller's Data Services Web team. There's a wealth of information available. It's all free of charge and will be updated annually. **FN**

To view the FAST report and study school district cost-effectiveness in your area, visit *www.fastexas.org*.

### FAST RESULTS

Among the school districts examined by the **FAST** review team:

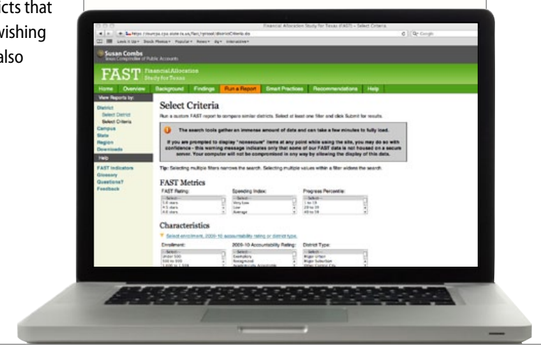
★★★★★
**3.8 percent** (43) earned a **5-star** rating;

★★★★
**19.8 percent** (224) earned a **4.5- or 4-star** rating;

★★★
**36.3 percent** (411) earned a **3.5- or 3-star** rating;

★★
**30.6 percent** (346) earned a **2.5- or 2-star** rating; and

★
**9.5 percent** (107) earned a **1.5- or 1-star** rating.



# The Oil Beneath the Oil

BY CLINT SHIELDS

Chip Groat
Professor,
Geological Sciences
University of Texas
at Austin

There's oil, deep in West Texas' Permian Basin — and plenty of it. After nearly 90 years of production, most of the basin's oil remains in the ground.

"Traditionally, you get between 20 and 40 percent of the oil in a reservoir, depending on the type of rock that surrounds it," says Chip Groat, a professor of Geological Sciences at the University of Texas at Austin.

Much of the basin's remaining oil, however, lies in residual oil zones (ROZs). These pools of oil lie *beneath* primary production zones, often separated from them by rock or brine reservoirs.

But Texans are reaching for that untouched crude. With a U.S. Department of Energy grant of nearly $1.2 million, scientists and students from the University of Texas of the Permian Basin (UTPB) are leading research into the use of enhanced oil recovery, or EOR, in residual oil zones. The most recent grant is the third UTPB has received for its oil recovery research.

"In the Permian Basin, we have primary oil production everywhere from 2,000 feet down to 15,000 feet," says Bob Trentham, director of UTPB's center for energy and economic diversification. "What we don't know is how deep we can recover oil, because there isn't much data on residual oil zones."

## FLOODING THE ZONE

EOR includes various techniques that can wring more oil out of a mature production area. The most common type of EOR used in the Permian Basin is $CO_2$ injection, a proven technology dating back almost 40 years.

As oil is produced, the pressure within the reservoir drops, making it more difficult for the remaining oil to flow toward the well. $CO_2$ injection floods the reservoir with the gas to repressurize it, encouraging further oil production. (See sidebar for more on oil recovery techniques.)

To better understand how EOR techniques could recover oil in a residual zone, researchers first have to understand how it got there.

"That's where we are right now with ROZs," Trentham says. "We need to understand them better and that's what this grant will help us do."

UTPB researchers, along with corporate partners Legado Resources and Melzer Consulting, will focus on developing ROZ data on a specific oilfield to build a better understanding of how to pull oil from it.

"We know the ROZ is there," Trentham says. "With data donated by our corporate partners, we can develop a picture of what the ROZ looks like, its characteristics, how it might flood better — all the things we need to know before we go blindly ahead and try to pull oil from it. $CO_2$ flooding has doubled the potential size of the recovery prize in the residual zones."

## OLD OILFIELDS, LIKE NEW

Reaching ROZs could greatly increase our estimates of oil reserves. Traditionally, when oil is discovered and the field is studied, producers estimate both the amount of oil "in place" and the recoverable amount, says UT-Austin's Groat.

"When a field is analyzed, you say we have 'X' million barrels in place," Groat says. "Reserves are the part that can be recovered using standard techniques. The rest of that oil in place is not considered part of the reserve because you can't get it out. If new techniques allow us to get to it, then it becomes part of the proven reserves. And it wouldn't be a new oil find. It'd just be old oil recovered more efficiently."

The state's signature type of crude oil, known as West Texas Intermediate (WTI), remains the major benchmark of crude oil in the Americas.

Adding to those reserves — and potentially lessening U.S. dependence on foreign oil — are among Trentham's goals. And the latest grant will help make it happen.

"We believe that we are the model for the rest of the country as far as how this should be done," he says. "There's huge potential for the Permian Basin as well as basins nationwide." **FN**

UTPB provides a variety of residual oil zone materials, including symposium discussion presentations and notes, Permian Basin maps and more, online at *www.residualoilzones.com*.

AT ITS PEAK IN **1972**,
THE TEXAS OIL INDUSTRY **PRODUCED** ABOUT
**3,000,000**
**BARRELS** PER DAY

## KEEP IT PUMPING

Pumping crude oil from the ground is done in three ways:

- **PRIMARY** — When an oil field is first tapped, gravity or the reservoir's natural pressure pushes oil to the well. Pumps and other implements can help bring oil to the surface. Typically, primary recovery can pull 10 to 20 percent of the oil from a field.
- **SECONDARY** — Over time, the original pressure in a primary zone subsides and production slows. Typically, water or gas is then injected into the oil field to drive oil to the well. In the case of water, however, the more that is pumped into a field, the more comes up with the oil, which leads to less recovered oil. Secondary production can claim an additional 10 to 30 percent of a field's available oil.
- **TERTIARY** — This type of recovery can include using $CO_2$, chemical or thermal injection to recover oil. It has been used in primary oil zones for years, but is now being explored as an option in developing residual oil zones. It is costly, however, and $CO_2$ in Texas is a "highly sought after commodity, not a waste product," says UTPB's Bob Trentham. Tertiary recovery can ultimately pull 30 to 60 percent of the original oil from a field.

## TEXAS OIL FACTS

TEXAS HAS MORE THAN
**149,000**
**OIL-PRODUCING WELLS**

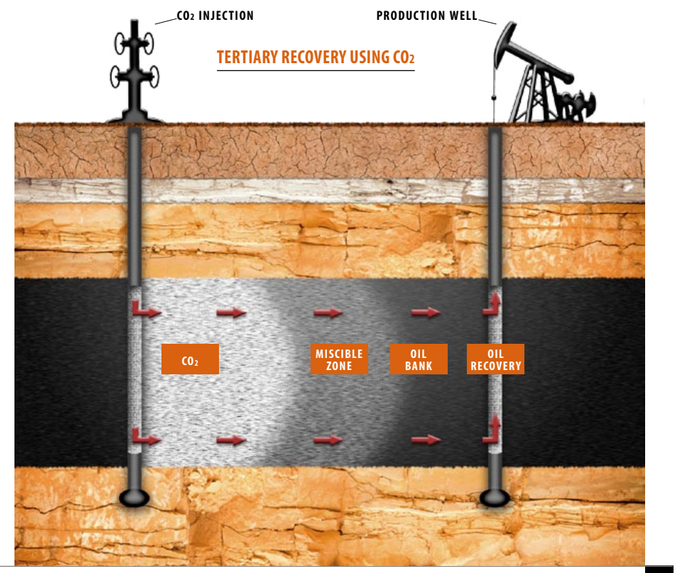

TEXAS HAS MORE THAN
**25%**
OF THE NATION'S
**PETROLEUM REFINING CAPACITY,**
AT MORE THAN
**4.7**
**MILLION**
**BARRELS** OF OIL PER DAY

THE LONE STAR STATE
PRODUCES ABOUT
**35**
**MILLION**
**BARRELS OF OIL EACH MONTH,**
**1/5**
OF ALL U.S. PRODUCTION

TEXAS' **5 BILLION BARRELS** IN
**CRUDE OIL RESERVES** REPRESENT MORE
THAN **24 PERCENT** OF THE U.S. TOTAL


THE TEXAS OIL AND NATURAL GAS INDUSTRY **EMPLOYS** AN
ESTIMATED **243,000** PEOPLE.

*Source: U.S. Energy Information Administration*



# Texas and the New Space Race

BY BRUCE WRIGHT


## *An Interview with Richard Garriot, Part III*

*In the last two issues of* Fiscal Notes*, we spoke with Richard Garriott, computer game pioneer, investor and private astronaut, about NASA's new initiative to place greater reliance on private contractors for space exploration, and what it might mean for Texas. In our final installment, we discuss Texas' prospects in the emerging private space industry — and Garriott's own plans for a unique new sport.*

**FN:** We've mentioned Dallas' Armadillo Aerospace. [See Part 2 of this interview at *FiscalNotes.com*.] And I believe that SpaceX has an engine test facility in Texas.

**Garriott:** They do.

**FN:** What else is happening in private space activity in Texas right now?

**Garriott:** There are a couple of even smaller rocket companies here in Texas.

And the same group of us that started the original X Prize, which was a $10 million prize for the first private vehicle to fly twice into space, put together the Google Lunar X Prize. Google's put up $25 million for the first private

*A rocket motor is put through its paces at the SpaceX test facility in McGregor, Texas.*

[unmanned] rover to travel across the moon and send back high-definition video. There are a number of teams competing based here in Texas.

There's no question that the skill set to compete exists in Houston. And that work force is either going to be reapplied somewhere or be laid off, you know, pretty soon [due to the conclusion of the Shuttle program].

And so now is the time for Texas to decide how to become competitive in this new arena. It's great that SpaceX has a test facility here in Texas. But SpaceX is based in L.A.

We need more companies *founded* here, in Texas. And we have the skills. We just have to encourage the formation of rocket development companies in Texas.

> "Now is the time for Texas to decide how to become competitive in this new arena."
>
> —Richard Garriott

**FN:** And how could Texas help with that? What would we do?

**Garriott:** Well, that's an interesting question. First I think it would start with a high-level vision statement, where someone, the governor perhaps, says look, Texas needs to be part of this new economy, like we're already doing with clean energy and a number of other things.

If we want to be a competitor in the new space economy, that would be where we need to start. Then you have to decide on a plan of action for how you can pull it off, what incentives you put in place and what companies you want to attract.

[It could involve] going to a lot of the prime contractors down there in Houston and saying, "Hey, the governor's going to host a roundtable where we discuss your skills and capabilities, and what we need to put together a new company that can take on the challenge of being a leader in the new space economy."

**FN:** What can be done to spur greater interest in the public? Can anything be done to revive the Apollo spirit?

**Garriott:** I think we do have a generation that honestly doesn't have a strong interest in space, which is very, very different from those of us who grew up during Apollo.

What I think is going to [revive interest] is what I call the barnstorming era of space, and that is almost upon us. We'll see many people leaving the Earth, starting to do wild, crazy, often dangerous and sometimes fatal things, *privately* — so it's not one of these things where every time we crash a shuttle we take everything offline for five years and debate who's at fault. It's a private individual taking their own private risks, and sometimes they succeed gloriously and sometimes they don't, gloriously.

And I think that within three or four years we're going to start seeing safe, rapid-fire opportunities for suborbital space tourism — not just from Virgin Galactic or Space Adventures, but from two or three other competitors that come out on our heels.

Right around that same time, or within a year of that, we're going to have companies like XCOR not only making suborbital hops, but also looking at high-speed point-to-point trips.

And so, just like in the barnstorming era of airplanes, we're going to see people starting to do clever, thoughtful, unique things with rockets.

As soon as this cost thing flips, which I think will happen in about 10 years, people are going to see entrepreneurs going and doing stuff in space and funding their own trips. They're going to go stay and live in space, not because they're wealthy or super scientists, not because they're backed by a government, but because they have kind of a cool idea, and somebody, some angel investor, gave them the $10 million they needed, which is not an outrageous amount of money to get behind an actual good idea for a business.

And as soon as that begins to happen, people are going to go, "Wait, I can do that too!"

Right now, students — even those who do think about space as being something they would love to do — very quickly realize the probabilities [of going into space] are so heavily stacked against them that they give up.

That's the main problem with a government space program: It makes spaceflight so rare that everyone just gives up. No one believes it's something they can personally, practically aspire to.

**FN:** Speaking of barnstorming, would you like to tell us a little about your future plans?

**Garriott:** Of course, I want to go back to space. But I spent most of my money taking this rocket ride. If I had the money I'd go every chance I could.

So I'm asking myself, how can I get back to space? And, of course, I'm looking forward to riding on a suborbital rocket, which is much more affordable — but that's only four or so minutes in space.

So I'd really like to do something a little more interesting. And I've concluded that "something" is space diving. What I mean by that is to ride a suborbital rocket up to somewhere between 50 and 100 kilometers, jump out wearing a spacesuit, and then, when you safely reenter the Earth's atmosphere and get down to a low enough altitude and slow enough speed, to deploy a traditional parachute and land on the ground like a skydiver.

Our partnership with Armadillo Aerospace makes this particularly feasible.

Photo Courtesy of Armadillo Aerospace

*At work in the Armadillo Aerospace shop.*

The Armadillo vehicle is basically a pogo stick — it goes straight up and it comes straight down, and you can put a crew capsule on top of it or not. You could, basically, lie on top with your spacesuit and your parachute, go up to space, and when the engines throttle down, step off. The spacesuit was your cabin, so to speak. You'd reenter without the rocket and parachute down.

So far, this is mostly speculation. But Armadillo and Space Adventures have talked about it. I have actually put money into the development of space diving suits, so it's something we're seriously pursuing.

**FN:** What do you think time frame is on that?

**Garriott:** Very similar to that for suborbital rockets in general. I think it's three or so years.

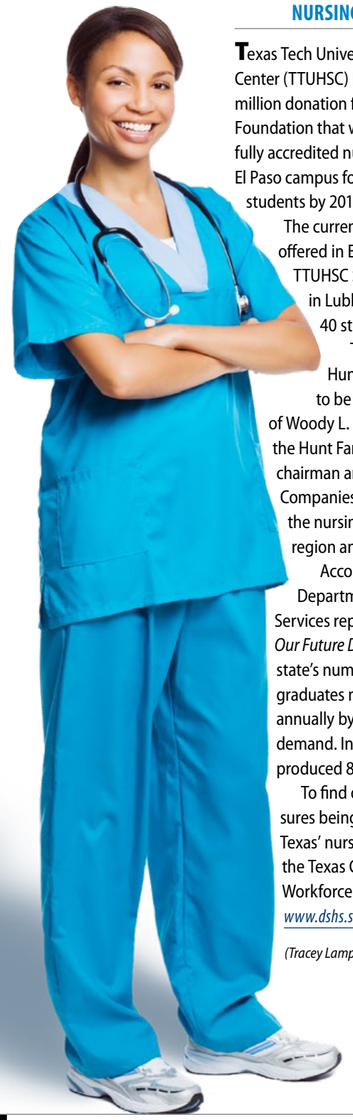
*Continued on page 13*

Photo Courtesy of Armadillo Aerospace

*An Armadillo Aerospace vehicle awaits testing.*

# Brief Bytes

## $10 MILLION TO TACKLE NURSING SHORTAGE



Texas Tech University Health Sciences Center (TTUHSC) has received a $10 million donation from the Hunt Family Foundation that will help develop a fully accredited nursing school on its El Paso campus for as many as 500 students by 2015.

The current nursing program offered in El Paso, through the TTUHSC School of Nursing in Lubbock, serves about 40 students.

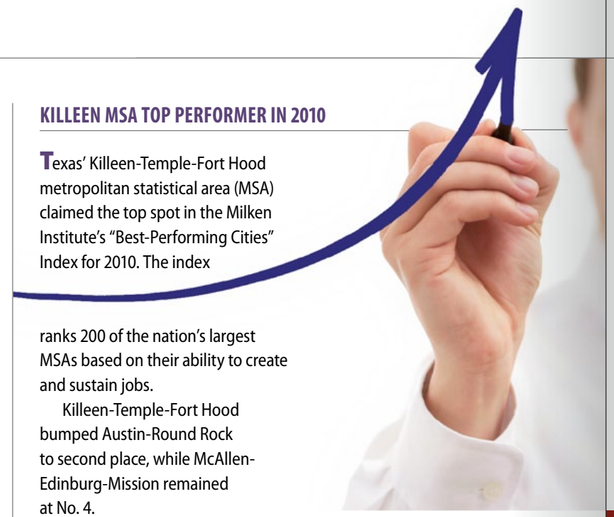
The new Gayle Greve Hunt School of Nursing, to be named for the wife of Woody L. Hunt, chairman of the Hunt Family Foundation and chairman and CEO of the Hunt Companies, will help shrink the nursing shortage for the region and the state.

According to a Texas Department of State Health Services report, *Texas Nursing: Our Future Depends on It,* the state's number of new nursing graduates must grow to 25,000 annually by 2020 to meet demand. In 2009, Texas schools produced 8,211 graduates.

To find out more about measures being taken to address Texas' nursing shortage, visit the Texas Center for Nursing Workforce Studies at www.dshs.state.tx.us/chs/cnws.

*(Tracey Lamphere)*

## KILLEEN MSA TOP PERFORMER IN 2010



Texas' Killeen-Temple-Fort Hood metropolitan statistical area (MSA) claimed the top spot in the Milken Institute's "Best-Performing Cities" Index for 2010. The index ranks 200 of the nation's largest MSAs based on their ability to create and sustain jobs.

Killeen-Temple-Fort Hood bumped Austin-Round Rock to second place, while McAllen-Edinburg-Mission remained at No. 4.

Killeen-Temple-Fort Hood's job growth ranked in the top 10 in 2009, but its overall performance was boosted by its first-place position in wage and salary growth over the five-year (2003-2008) and one-year (2007-2008) periods Milken examined for the index. It also ranked third nationally in year-over-year job growth in the year ending April 2010.

"Our region's economic success is due in no small part to our balance," says John Crutchfield, president of the Killeen Chamber of Commerce. "We are blessed with robust manufacturing on the east side of the region, robust service industries — primarily in defense contracting — on the west side of the region, a robust medical industry throughout the region and a growing educational complex."

Fort Hood provides the region with $7.1 billion annually in economic activity and a constant supply of work force talent in the form of military retirees and spouses.

"We enjoy a location central to the state with multiple transportation options," Crutchfield says, "and we have worked very hard to keep our cost of living low, to keep Fort Hood competitive for military investment."

For a complete list of the Best Performing Cities, including the biggest gainers and decliners, visit http://bestcities.milkeninstitute.org.

*(Tracey Lamphere)*

**MILKEN INSTITUTE'S 10 BEST-PERFORMING METRO AREAS, 2010**

| |
|---|
| **1. Killeen-Temple-Fort Hood** |
| **2. Austin-Round Rock** |
| 3. Huntsville, AL |
| **4. McAllen-Edinburg-Mission** |
| 5. Kennewick-Richland-Pasco, WA |
| 6. Washington-Alexandria-DC, VA |
| 7. Raleigh-Cary, NC |
| 8. Anchorage, AK |
| **9. El Paso** |
| **10. Houston-Sugar Land-Baytown** |

*Source: The Milken Institute*

**GET CONNECTED**

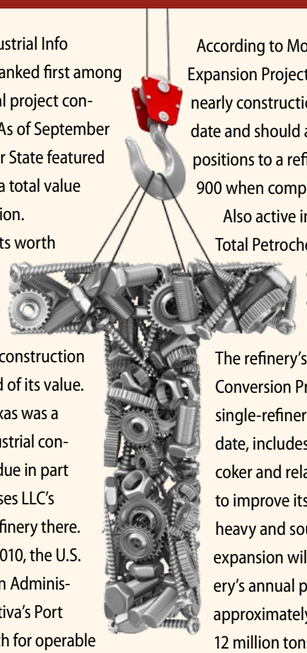
**Follow us on @txcomptroller to get the latest news and economic analysis.**

## TEXAS FIRST IN INDUSTRIAL CONSTRUCTION

According to Industrial Info Resources, Texas ranked first among states for industrial project construction in 2010. As of September 2010, the Lone Star State featured 184 projects with a total value exceeding $26 billion.

With 98 projects worth $9 billion, second-ranked California trailed Texas with roughly half of its construction activity and a third of its value.

Port Arthur, Texas was a major hub for industrial construction in 2010, due in part to Motiva Enterprises LLC's expansion of its refinery there. As of September 2010, the U.S. Energy Information Administration ranked Motiva's Port Arthur refinery 14th for operable capacity, capable of processing 285,000 barrels per day (bpd) of crude oil. When the expansion is complete, the Motiva refinery will have a capacity of 600,000 bpd, making it the nation's leader.



According to Motiva, the Crude Expansion Project has created nearly construction 6,500 jobs to date and should add 300 full-time positions to a refinery staff of about 900 when completed in 2012.

Also active in Port Arthur is a Total Petrochemicals refinery capable of processing 174,000 bpd of crude oil. The refinery's $2.2 billion Deep Conversion Project, its biggest single-refinery investment to date, includes a 50,000 bpd coker and related equipment to improve its processing of heavy and sour crude oil. The expansion will raise the refinery's annual product output to approximately 12 million tons.

This project employed 4,700 construction workers as of October 2010, and will add at least 60 jobs upon completion in 2011.

*(Meghan Vail)*

*CONTINUED FROM PAGE 11*

# Texas and the New Space Race

"That's the main problem
with a government space program:
It makes spaceflight
so rare that everyone just gives up.
No one believes it's something they can aspire to."

—Richard Garriott
entreprenuer, private astronaut

**FN:** Finally, what would be your advice to young Texans who are interested in exploring careers in private space?

**Garriott:** I think the good news about careers in space these days is how many new opportunities are going to be unfolding.

I believe that the democratization of access to space, which comes through the privatization of the tools needed to reach space, is going to create an explosion of new and fascinating job opportunities in everything from building hardware to operating experiments in space.

To get there, we're going to have to go through a tumultuous period of realigning a lot of the traditional aerospace companies into a more commercially competitive arrangement. The result of that, though, will be that employment in this sector will go up, and I believe significantly.

And that will be especially true for young people who have the vision and passion for doing things in a new way. I think the things that will be rewarded in this next era will be the tasks that people once thought weren't possible.

Five or 10 years ago, I don't think anybody would have believed that Armadillo Aerospace would be flying a rocket that could reach even suborbital space six times in a day with no refurbishment other than refueling.

I think that people had never seriously thought that the Skylon team, which is trying to create a single-stage orbital vehicle, had a prayer, and now they're slowly convincing their skeptics.

And there's going to be another X Prize for energy-beamed propulsion, where you don't have to take all that fuel with you as you launch. Both fairly traditional rockets as well as fairly exotic rockets will now begin to emerge.

**FN:** Thank you for speaking with us today.

**Garriott:** My pleasure. **FN**

Read the first two parts of this interview at www.FiscalNotes.com.

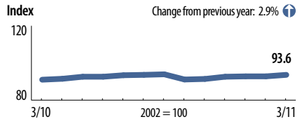
# Texas by the Numbers

For detailed statistics on the Texas economy, check the Comptroller's website at **www.TexasAhead.org**

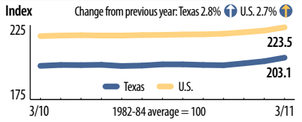
**Key Texas Economic Indicators -** Texas total nonfarm employment increased by 32,400 jobs from Febrary to March. Between March 2010 and March 2011, Texas gained 251,100 jobs. Over the past year, Texas added jobs in most sectors, including construction, manufacturing, mining and logging, leisure and hospitality, financial activities, professional and business services, educational and health services, and government.

## INDEXES

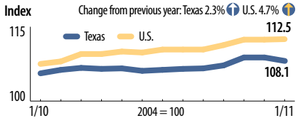
### Industrial Production Index



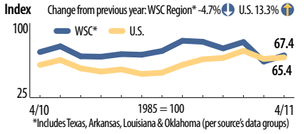

### Consumer Price Index




### Leading Economic Indicators Index



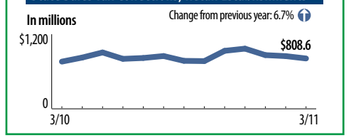

### Consumer Confidence Index




*Includes Texas, Arkansas, Louisiana & Oklahoma (per source's data groups)

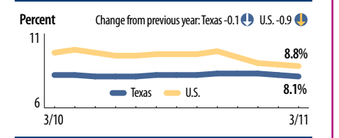
## SALES TAX

### State Sales Tax Collections, Retail Establishments

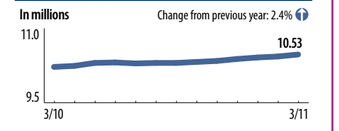



## EMPLOYMENT

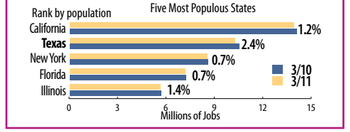
### Unemployment Rate




### Nonfarm Employment

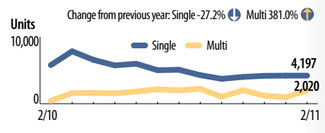



### Change in Nonfarm Employment

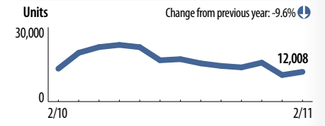



## REAL ESTATE

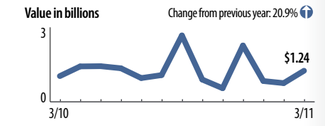
### Housing Permits



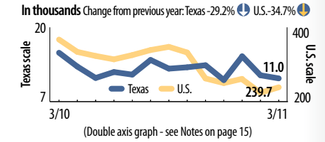

### Existing Single-Family Home Sales




### Texas Non-Residential Building Construction Contracts




### Mortgage Foreclosures




(Double axis graph - see Notes on page 15)

## Texas Production and Consumption Indicators

| DATE | Crude Oil Production Value (MILLIONS) | Natural Gas Production Value (MILLIONS) | Active Oil & Gas Drilling Rigs Units | Motor Fuels Taxed Gasoline (MILLIONS OF GALLONS) | Motor Fuels Taxed Diesel (MILLIONS OF GALLONS) | Median Sale Price, Existing Single-family Home Dollars | Auto Sales Net Value (MILLIONS) | Cigarettes Taxed Packages of 20 (MILLIONS) |
|---|---|---|---|---|---|---|---|---|
| **2009** | $18,380.2 | $10,021.3 | 5,178.0 | 993.0 | 289.7 | $144,792 | $34,792.6 | 949.9 |
| **2010** | 14,309.3 | 7,283.3 | 4,994.1 | 996.6 | 303.9 | 146,229 | 21,955.1 | 630.3 |
| **MAR-10** | 2,209.9 | 1,244.6 | 593 | 913.6 | 273.8 | 144,000 | 3,356.2 | 87.2 |
| **APR-10** | 2,252.9 | 1,084.8 | 633 | 1,032.9 | 327.8 | 146,700 | 3,011.3 | 81.8 |
| **MAY-10** | 2,011.1 | 1,158.7 | 647 | 1,002.8 | 315.8 | 148,100 | 2,852.6 | 75.9 |
| **JUN-10** | 1,916.3 | 1,156.4 | 663 | 1,060.4 | 313.5 | 152,300 | 3,490.5 | 81.0 |
| **JUL-10** | 2,071.2 | 1,254.7 | 676 | 1,028.3 | 319.0 | 154,500 | 3,460.0 | 81.2 |
| **AUG-10** | 2,155.5 | 1,301.5 | 714 | 1,034.2 | 311.4 | 153,100 | 3,587.7 | 81.4 |
| **SEP-10** | 2,085.8 | 1,148.47 | 721 | 1,053.6 | 310.2 | 146,800 | 3,432.6 | 87.6 |
| **OCT-10** | 2,367.0 | 1,257.06 | 717 | 1,001.6 | 318.5 | 144,800 | 3,325.9 | 82.4 |
| **NOV-10** | 2,395.6 | 1,208.71 | 734 | 1,031.7 | 322.2 | 146,400 | 3,231.1 | 79.5 |
| **DEC-10** | 2,706.4 | 1,504.08 | 746 | 1,044.4 | 308.8 | 150,800 | 3,265.1 | 71.4 |
| **JAN-11** | 2,740.5 | 1,375.57 | 736 | 962.7 | 314.8 | 139,000 | 3,225.5 | 66.4 |
| **FEB-11** | 2,173.5 | | 747 | 965.0 | 304.3 | 145,800 | 3,265.7 | 73.8 |
| **MAR-11** | | | 748 | 884.4 | 284.7 | | | 91.0 |



## March Cash Condition[1]

| (Amounts in millions) | General Revenue | Other Funds | Total Cash |
|---|---|---|---|
| **BEGINNING BALANCE MARCH 1, 2011** | **$3,065.7** | **$22,083.6** | **$25,149.3** |
| Revenue/Expenditures | | | |
| Revenue | 6,159.7 | 2,340.5 | 8,500.2 |
| Expenditures | 6,131.4 | 2,994.0 | 9,125.4 |
| Net Income (outgo) | $28.3 | $-653.5 | $-625.2 |
| Net Interfund Transfers and Investment Transactions | $-496.5 | $580.9 | $84.4 |
| Total Transactions | -468.2 | -72.6 | -540.8 |
| **END CASH BALANCE MARCH 31, 2011[2]** | **$2,597.5** | **$22,011.0** | **$24,608.5** |

[1] Cash stated is from the Comptroller's Uniform Statewide Accounting System (USAS) and will vary from the amounts reflected in the cash accounts of the Treasury Operations Division of the Comptroller's office due to timing differences. Net amounts shown (less refunds) exclude funds that are authorized to be held outside the State Treasury and are not processed through USAS. Suspense and Trust Funds are included, as are unemployment compensation trust funds collected by the state but held in the Federal Treasury. Totals may not add due to rounding.

[2] The ending General Revenue Fund balance includes $7.4 billion derived from the sale of cash management notes.

## State Revenue/All Funds[1]

| (Amounts in millions) | Monthly Revenue March 2011 | Fiscal Year-to-Date March 2011 Revenue | % Change YTD/YTD |
|---|---|---|---|
| **TAX COLLECTIONS BY MAJOR TAX** | | | |
| Sales Tax | $1,616.3 | $12,070.6 | 8.9% |
| Oil Production Tax | 96.2 | 729.7 | 25.7 |
| Natural Gas Production Tax | 112.6 | 624.9 | 91.0 |
| Motor Fuel Taxes | 229.3 | 1,785.6 | 3.9 |
| Motor Vehicle Sales Tax | 285.8 | 1,671.9 | 14.4 |
| Franchise Tax | 173.0 | -36.1 | -163.3 |
| Cigarette & Tobacco Taxes | 137.8 | 852.4 | 10.7 |
| Alcoholic Beverages Tax | 69.3 | 483.6 | 6.4 |
| Insurance Companies Tax | 386.8 | 786.1 | -1.3 |
| Utility Taxes[2] | 1.8 | 212.7 | -1.2 |
| Inheritance Tax | 0.0 | 0.8 | 436.7 |
| Hotel/Motel Tax | 31.1 | 197.9 | 13.7 |
| Other Taxes3 | 1.1 | 554.7 | 146.6 |
| **TOTAL TAX COLLECTIONS** | **$3,141.2** | **$19,934.7** | **11.6%** |
| **REVENUE BY RECEIPT TYPE** | | | |
| Tax Collections | $3,141.2 | $19,934.7 | 11.6% |
| Federal Income | 3,385.7 | 24,627.3 | 7.3 |
| Interest and Investment Income | 163.7 | 748.4 | -8.1 |
| Licenses, fees, permits, fines, | 376.4 | 4,352.7 | 8.8 |
| Contributions to Employee Benefits | 535.3 | 3,285.0 | 7.1 |
| Sales of Goods and Services | -64.7 | 108.0 | -52.7 |
| Land Income | 84.3 | 695.7 | 82.3 |
| Net Lottery Proceeds[4] | 181.5 | 983.5 | 0.2 |
| Other Revenue Sources | 696.8 | 5,079.5 | 3.9 |
| **TOTAL NET REVENUE** | **$8,500.2** | **$59,814.7** | **8.4%** |

[1] Excludes revenues for funds that are authorized to be held outside the State Treasury and are not processed through USAS. Totals may not add due to rounding.

[2] Includes the utility, gas utility administration and public utility gross receipts taxes.

[3] Includes the cement and sulphur taxes and other occupation and gross receipt taxes not separately identified.

[4] Gross sales less retailer commissions and the smaller prizes paid by retailers.

## State Expenditures/All Funds[1]

| (Amounts in millions) | Monthly Expenditures March 2010 | Fiscal Year-to-Date March 2011 Expenditures | % Change YTD/YTD |
|---|---|---|---|
| **BY OBJECT** | | | |
| Salaries and Wages | $914.2 | $6,411.9 | 0.7% |
| Employee Benefits/ Teacher Retirement Contribution | 902.3 | 6,011.4 | 4.1 |
| Supplies and Materials | 85.8 | 577.6 | 0.7 |
| Other Expenditures | 387.2 | 2,134.7 | 12.1 |
| Public Assistance Payments | 4,113.7 | 27,504.0 | 3.7 |
| Intergovernmental Payments: | | | |
| Foundation School Program Grants | 677.2 | 11,145.1 | 9.9 |
| Other Public Education Grants | 1,332.4 | 4,556.3 | 11.4 |
| Grants to Higher Education | 98.6 | 722.2 | 8.7 |
| Other Grants | 274.2 | 1,871.4 | 2.2 |
| Travel | 12.1 | 85.5 | -3.9 |
| Professional Services and Fees | 177.7 | 1,303.6 | 0.6 |
| Payment of Interest/Debt Service | 346.6 | 789.9 | 44.0 |
| Highway Construction and Maintenance | 248.1 | 2,069.2 | 15.6 |
| Capital Outlay | 48.1 | 303.3 | -6.4 |
| Repairs and Maintenance | 59.3 | 446.8 | -3.0 |
| Communications and Utilities | 46.1 | 302.8 | 4.0 |
| Rentals and Leases | 24.3 | 167.0 | -2.4 |
| Claims and Judgments | 10.9 | 62.9 | -25.8 |
| Cost of Goods Sold | 39.4 | 285.1 | 14.8 |
| Printing and Reproduction | 4.6 | 25.6 | -5.3 |
| **TOTAL NET EXPENDITURES** | **$9,125.4** | **$66,776.2** | **5.8%** |
| **BY FUNCTION** | | | |
| General Government | | | |
| Executive | $704.1 | $4,581.0 | 18.4% |
| Legislative | 12.7 | 80.2 | 2.2 |
| Judicial | 22.9 | 153.6 | -3.2 |
| Subtotal | 739.7 | 4,814.8 | 17.2 |
| Health and Human Services | 4,085.4 | 26,491.1 | 2.6 |
| Public Safety and Corrections | 398.5 | 2,767.9 | -4.8 |
| Transportation | 448.3 | 3,681.5 | 11.2 |
| Natural Resources/Recreational Services | 140.0 | 1,038.3 | -4.4 |
| Education | 2,051.3 | 21,083.1 | 7.2 |
| Regulatory Agencies | 22.9 | 208.7 | -3.4 |
| Employee Benefits | 787.1 | 5,279.6 | 6.0 |
| Debt Service—Interest | 346.6 | 789.9 | 44.0 |
| Capital Outlay | 48.1 | 303.3 | -6.4 |
| Lottery Winnings Paid[2] | 57.6 | 317.9 | 94.6 |
| **TOTAL NET EXPENDITURES** | **$9,125.4** | **$66,776.2** | **5.8%** |

[1] Excludes expenditures for funds that are au thorized to be held outside the State Treasury and are not processed through USAS. Totals may not add due to rounding.

[2] Does not include payments made by retailers. Previously shown as "Other expenditures."

Some revenue and expenditure items have been reclassified, changing year-to-date totals. The ending cash balance is not affected because changes reflected in "total net revenues" and "total net expenditures" offset changes in "net interfund transfers and investments transactions" in the cash condition table.

Revenues and expenditures are reported for the most recent month available and as a running total for the current fiscal year-to-date. In addition, year-to-date figures are compared with the same period in the last fiscal year. These comparisons are reported as percentage changes, which may be positive or negative (shown by a minus sign).

Trust fund transactions are included within revenues and expenditures in the "all funds" presentations. Trust funds are not available to the state for general spending.

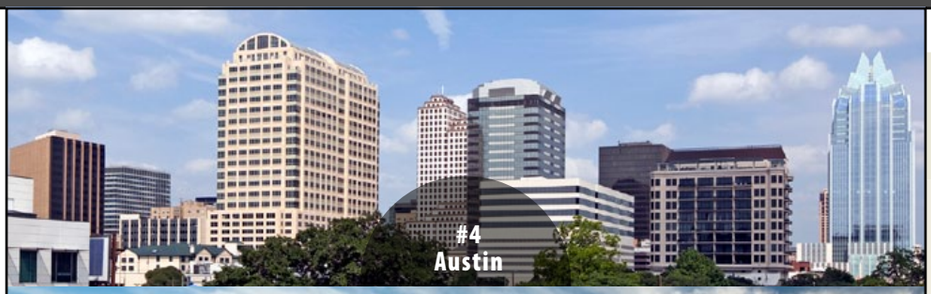
### NOTES:

Crude oil and natural gas figures are net taxable values. Gasoline gallons include gasohol. Auto sale values are calculated from motor vehicle taxes collected on new and used vehicle sales. All figures are seasonally adjusted, except for sales tax collections; rigs; consumer price; housing permits/sales/prices; and consumer confidence. Figures are based on the most recent available data. Annual figures are for calendar years. [‡ Double axis graphs: Graphs with two vertical axes show values for Texas on the left and values for the U.S. on the right. This method shows trends more clearly over the last year when data values are substantially different at state and national levels.]

### SOURCES:

**KEY TEXAS ECONOMIC INDICATORS:**
Consumer Price Index, Change in Nonfarm Employment: U.S. Bureau of Labor Statistics
Consumer Confidence Index: The Conference Board
Leading Economic Indicators Index: Texas Comptroller of Public Accounts, The Conference Board
Unemployment Rate: Texas Workforce Commission, U.S. Bureau of Labor Statistics
Nonfarm Employment: Texas Workforce Commission
State Sales Tax Collections, Retail Establishments: Texas Comptroller of Public Accounts
Housing Permits, Existing Single-family Home Sales: The Real Estate Center at Texas A&M University
Industrial Production Index: Federal Reserve Bank of Dallas
Contract Value, Non-Residential Building Construction: McGraw-Hill
Mortgage Foreclosures: RealtyTrac

**TEXAS PRODUCTION AND CONSUMPTION INDICATORS:**
Crude Oil, Natural Gas, Motor Fuels, Auto Sales, Cigarettes: Texas Comptroller of Public Accounts
Active Oil & Gas Drilling Rigs: Baker-Hughes Incorporated
Median Sale Price, Existing Single-family Home: The Real Estate Center at Texas A&M University





## TEXAS COMMERCIAL REAL ESTATE LOOKING UP

Austin ranked fourth, Houston ranked eighth and Dallas 12th out of more than 50 U.S. cities listed in the Price Waterhouse Coopers and Urban Land Institute's Emerging Trends in *Real Estate 2011* report. This annual forecast identifies the nation's hottest prospects for commercial real estate investment.

The report cited Austin as one of the nation's "brainpower bastions," and noted Houston's "intellectual capital and talent in the global energy business." Despite sagging retail and a soft real estate market, Dallas "remains an important intersection for global commerce," with Dallas/Fort Worth International Airport tabbed as the area's most important asset.

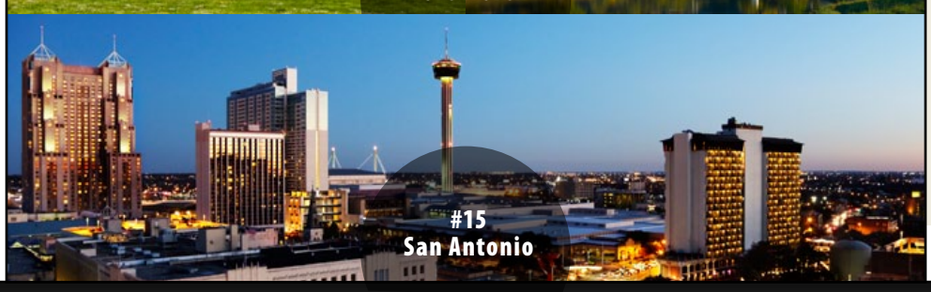
To download a copy of the report, visit the Urban Land Institute at *www.uli.org/*.

*(Tracey Lamphere)*

### TOP COMMERCIAL REAL ESTATE MARKETS FOR 2011

1. Washington, D.C.
2. New York
3. San Francisco
4. **AUSTIN**
5. Boston
6. Seattle
7. San Jose
8. **HOUSTON**
9. Los Angeles
10. San Diego
11. Denver
12. **DALLAS-FORT WORTH**
13. North New Jersey
14. Orange County, Calif.
15. **SAN ANTONIO**

*Source: Emerging Trends in Real Estate 2011, Price Waterhouse Coopers and the Urban Land Institute*


**Susan Combs**
Texas Comptroller of Public Accounts

*Fiscal Notes* is one of the ways the Comptroller's office strives to assist taxpayers and the people of Texas. The newsletter is a by-product of the Comptroller's constitutional responsibilities to monitor the state's economy and to estimate state government revenues.

*Fiscal Notes* also provides a periodic summary of the financial statements for the State of Texas.

Articles and analysis appearing in *Fiscal Notes* do not necessarily represent the policy or endorsement of the Texas Comptroller of Public Accounts. Space is devoted to a wide variety of topics of Texas interest and general government concern.

**STAFF**

DELANE CAESAR
DIRECTOR OF DATA SERVICES DIVISION

**Creative Directors**
Beth Hallmark and Dan Lynch

**Graphics Team Leader**
Dwain Osborne

**Art Direction, Layout & Design**
Duana Gill, Brandy Bianco, Sherryl Orsak

**Staff Photography**
Raul Santos, Michael Castellon

**Photo Retouching & Illustration**
Raul Santos

**Editorial Team Leader**
Karen Hudgins

**Editor**
Bruce Wright

**Staff Writers**
David Bloom, Michael Castellon, Tracey Lamphere, Gerard MacCrossan, Clint Shields, Mark Wangrin, Meghan Vail

**Web Publications Coordinator**
Julie Lewis

**E-communications Coordinator**
Michael Castellon

**FIELD OFFICES**

Comptroller field offices are located in Abilene, Amarillo, Austin, Beaumont, Brownsville, Bryan, Corpus Christi, Dallas, Denton, El Paso, Fort Worth, Houston, Laredo, Lubbock, Lufkin, McAllen, Odessa, San Angelo, San Antonio, Sherman, Tyler, Victoria, Waco and Wichita Falls, as well as Chicago, Los Angeles, New York and Tulsa.

**HOW TO REACH US**

Toll-free telephone line:
(800) 531-5441, ext. 3-3116; in Austin, 463-3116.

Send questions or comments to fiscal.notes@cpa.state.tx.us.

**COMPTROLLER'S WEBSITE**

Window on State Government is on the World Wide Web at www.window.state.tx.us. Online subscriptions, renewals or cancellations of *Fiscal Notes* may be entered at *https://www.window.state.tx.us/fnotes/*
(note: the final slash must be included in the address).



Texas Comptroller of Public Accounts
Publication #96-369,
May 2011

FISCAL NOTES

A Review of the Texas Economy from the Office of Susan Combs, Texas Comptroller of Public Accounts



Online subscriptions, renewals or cancellations of *FISCAL NOTES* may be entered at
https://www.window.state.tx.us/fnotes/
(note: the final slash must be included in the address).
Send questions or comments to fiscal.notes@cpa.state.tx.us.

Fax: (512) 463-4226 or (800) 252-3620

Or write:
*FISCAL NOTES*
Texas Comptroller of Public Accounts
Data Services Division
111 E. 17th St., Suite 301, Austin, TX 78774-0100

For more information, call (800) 531-5441, ext. 3-3116; or 463-3116 in Austin.

Window on State Government is on the World Wide Web at www.window.state.tx.us.